

STATE OF MICHIGAN
IN THE SUPREME COURT

CITIZENS INSURANCE COMPANY,

Plaintiff/Appellant,

S.C. No. 130099

v

COA No. 262759

PRO-SEAL SERVICE GROUP, INC.,
d/b/a PRO-SEAL, INC., a Michigan
corporation,

L.C. No. 04-056953-CZ

Defendant/Appellee.

and

FLOWERVE CORPORATION, a New York corporation,
FLOWERVE MANAGEMENT COMPANY, a
Delaware corporation, SETH SHORT and
RANDY QUINCY,

Defendants,

and

PRO-SEAL SERVICE GROUP, INC.,
d/b/a PRO-SEAL, INC., a Michigan
corporation,

Counter-Plaintiff,

v

CITIZENS INSURANCE COMPANY,

Counter-Defendant.

CITIZENS' REPLY BRIEF IN SUPPORT OF
APPLICATION FOR LEAVE TO APPEAL

PROOF OF SERVICE

130099
reply

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A. Pro-Seal's Response supports Citizens' request for this Court's review.

Pro-Seal's response to Citizens' application contains so many flaws and inaccuracies that the 10-page limit for reply briefs precludes Citizens from addressing all of them—much less the distinguishing features of the cases cited in its response and its “appendix” of cases (most if not all of which are materially distinguishable). Citizens will focus on the errors that it believes are most relevant to the Court's decision whether to grant leave. Before doing so, however, Citizens wishes to note a number of areas in which Pro-Seal's response, on its face, lends support to Citizens' position that this Court should review the Court of Appeals opinion.

First, Pro-Seal acknowledges that there is a very large body of case law in this area, including a split of authority on the applicability of the pertinent definition of “advertising injury” in the Citizens excess policy. Pro-Seal also concedes that the Court of Appeals opinion is the only published opinion in Michigan addressing whether trademark or trade dress claims are covered under a standard commercial general liability (CGL) policy. (Pro-Seal's Response (hereinafter, “Resp”), p 14). Despite acknowledging that these issues are frequently litigated, and that there is not a single Michigan opinion to provide guidance, save the one at issue, Pro-Seal contends that Citizens' assertion that the case involves legal principles of major significance to Michigan jurisprudence is “an unfounded exaggeration.” (Resp., pp iv-v). As support, Pro-Seal contends that most of the coverage disputes over claims under the Lanham Act are resolved in federal court. Whether or not that is true, it is irrelevant. The issue of whether a CGL policy provides coverage for allegations of trademark or trade dress violations is an issue of state contract law, not federal law. Federal courts would have jurisdiction over such disputes only if there is diversity of citizenship, and would apply state law to resolve them.

Pro-Seal also correctly notes that the Court of Appeals found that the “substance of the

Flowserve Complaint included allegations that would have permitted recovery based upon the theory of trade dress infringement.” (Resp, p v-vi). Yet, Pro-Seal appears to agree with Citizens that the allegations of the Flowserve complaint, in fact, do not assert a claim of trade dress infringement. After paraphrasing pertinent portions of the Flowserve complaint (see Resp, pp 4-5), which appear to be the same portions that the Court of Appeals believed asserted a trade dress infringement claim (Ct App Op, pp 4-5), Pro-Seal concedes that the allegations do not really assert trade dress infringement:

Although a person who is not familiar with trademark or trade dress law may consider the above paragraph sufficient to sustain an allegation of trade dress infringement or a Lanham Act violation, exactly the opposite is true. There is no infringement or violation as the customer who owned both the product and the packaging has the authority to repair the product to its own specifications and may use the re-usable shipping container for repair purposes. Pro-Seal has a complete defense to the allegations. A good analogy would be packing a Gateway computer in its original distinctive box and shipping it to a repair shop. After fixing the computer, the repair shop may re-pack the computer into the same box and ship it back to the customer.

(Resp, p 5). Citizens wholeheartedly agrees with Pro-Seal on this point, which is that the allegations that the Court of Appeals believed asserted trade dress infringement in fact do not.¹ Pro-Seal’s argument is that the Flowserve complaint, while not explicitly pleading a trade dress violation, misleadingly *appears to* do so (but in actuality does not), and, therefore, Citizens was obligated to defend. This argument is without merit, if not frivolous, on its face. Because an insurer’s duty to defend is based not on how the underlying complaint might be falsely perceived

¹ By finding that allegations of trademark infringement, counterfeiting, and use of a crate with a Flowserve label, without more, pled a claim of trade dress infringement, the Court of Appeals opinion, respectfully, exemplifies the type of “[un]familiar[ity] with trademark or trade dress law” to which Pro-Seal refers. *See also* fn 2, *infra*, for the requirements for pleading trade dress infringement. Pro-Seal’s apparent agreement that the Flowserve Complaint did not actually allege trade dress infringement demonstrates powerfully that this Court should reverse or, at a minimum, review the Court of Appeals opinion—particularly since Pro-Seal does not, and cannot, cite a decision from any jurisdiction that agrees with the Court of Appeals either.

by a person unfamiliar with the claim being pled, but on what is actually alleged, and because, as even Pro-Seal appears to agree, the Flowserve complaint does not allege trade dress infringement, there is no duty to defend.²

But what is perhaps most revealing about Pro-Seal's response is its outright failure to address the main errors in the Court of Appeals Opinion pointed out in Citizens' application. Citizens first explained that the Court erred in finding that allegations of trademark infringement "encompass" trade dress infringement, and that the Flowserve Complaint actually did plead trade dress infringement (Application, p 16-20). Citizens cited three on-point cases that reached the conclusion opposite of the Court of Appeals': *Central Mut Ins Co v StunFence, Inc*, 292 F Supp 2d 1072 (ND Ill, 2003); *NGK Metals Corp v Nat Union Fire Ins Co*, 2005 WL 1115925 (ED Tenn, April 29, 2005) (Application Exhibit G); and *Ohio Cas Ins Co v Albers Medical, Inc*, 2005 WL 2319820 (WD Mo, September 22, 2005) (Application Exhibit H). Pro-Seal addresses none of them, and cites no case that supports the result reached by Court of Appeals—which is not surprising because there is none. Second, Citizens argued that the Court of Appeals' finding that the supposed trade dress violations occurred in an advertisement, which is incorrect even under the ordinary meaning of "advertisement," certainly cannot be reconciled with the definition of "advertisement" provided in the Citizens CGL Policy (Application, pp 21-26). Pro-Seal makes no attempt to address that argument. Third, Citizens pointed out that the Court of Appeals

² Pro-Seal seems to argue later in its response that Flowserve did allege trade dress infringement (See, e.g., Resp, pp 22-23). Its earlier position, that Flowserve did not allege trade dress infringement, is the correct one. To plead a claim of trade dress infringement, one must allege that (1) the claimed trade dress is non-functional; (2) the claimed trade dress has secondary meaning; and (3) there is a likelihood of confusion between the plaintiff's goods and the defendant's. See *Yurman Design, Inc v PAJ, Inc*, 262 F3d 101, 115-16 (CA 2, 2001); *Clicks Billiards Inc v Sixshooters Inc*, 251 F3d 1252, 1258 (CA 9, 2001). A plaintiff must also offer "a precise expression of the character and scope of the claimed trade dress." *Landscape Forms, Inc v Columbia Cascade Co*, 113 F3d 373, 381 (CA 2, 1997). Flowserve plainly did not allege a trade dress violation, and the Court of Appeals clearly erred in finding that it did.

Opinion effectively nullifies the requirement of a causal connection between an advertising injury and an advertisement in the context of trade dress infringement (Application, pp 26-29). Pro-Seal not only fails to dispute this, it effectively urges precisely this result. (See, e.g., Resp, p 18, where Pro-Seal argues that all packaging and labeling is both trade dress and advertisement, and all Lanham Act violations are advertisement).

Rather than deal with the Court of Appeals' errors head-on, Pro-Seal's response attempts to obfuscate the issues, primarily by conflating the two policies and haphazardly arguing various points without ever explaining how the pertinent language of either policy, considered in isolation, provides coverage. This tactic enables Pro-Seal to declare (albeit incorrectly³), and use as its theme throughout the response, that there is a "great body of law" that supports a finding of coverage when the only cases to which Pro-Seal points for that proposition are cases that construed the "misappropriation of advertising ideas . . ." language from the excess policy that the Court of Appeals never addressed. The very first point Pro-Seal's response purports to make is that the Court of Appeals Opinion is the "same decision" that has been reached in numerous other jurisdictions (Resp., p iv)—a statement that could not be further from the truth. The fact of the matter is that there is not a single case in the country that can be cited as squarely supporting the Court of Appeals' holding that the allegations of trademark infringement in the Flowserve Complaint trigger coverage under the Citizens CGL Policy. Nor is this surprising, since the Court of Appeals Opinion, both as to its finding that the underlying complaint alleged trade dress infringement and its finding that that infringement was alleged to be in an "advertisement" as

³ As set forth in Section C. below, the body of law to which Pro-Seal points does not even support a finding of coverage under the excess policy in this case because the alleged trademark infringement is not alleged to have occurred in the "course of advertising."

defined in the Citizens CGL Policy, is clearly erroneous.⁴ As hard as Pro-Seal tries to argue otherwise, the reality is that the Court of Appeals Opinion stands alone in its conclusion that allegations of trademark infringement such as the ones at bar, unaccompanied by allegations of advertising, trigger a defense obligation under the Citizens CGL form.

Pro-Seal's acknowledgement that this case presents frequently-litigated issues that are of first impression in Michigan, combined with (1) its apparent concession that the Court of Appeals erred in finding that a trade dress infringement claim was pled in the underlying complaint, and (2) its inability otherwise to defend the Court of Appeals Opinion, demonstrate that this Court should grant leave to appeal and review the Court of Appeals Opinion.

B. There is no coverage under the Citizens CGL Policy

Pro-Seal's defense of the Court of Appeals' holding that coverage exists under the Citizens CGL Policy, which is set forth in its *second* argument (Resp, pp 17-23), begins by asserting a variety of arguments for the proposition that the Flowserve Complaint alleges trade dress infringement. It does not, as Pro-Seal itself aptly explained earlier in its response (See p 2 above). Notwithstanding the generic reference in the Flowserve Complaint to 15 USC §1125(a) (which is the statutory vehicle for both trademark and trade dress infringement claims (which explains why Flowserve cited it in connection with its trademark infringement allegations)), and regardless of whether the "Federal Rules of Civil Procedure" would have allowed for the

⁴ As one commentator explained in 2001:

"To date, no reported decision has addressed the issue whether the 1998 CGL covers losses resulting from a trademark infringement suit. However, the 1998 CGL clearly states that it covers only infringement of another's copyright, trade dress, or slogan, so that courts will no doubt be reluctant to construe "personal and advertising injury" to include trademark infringement."

introduction of evidence of trade dress infringement,⁵ the Flowserve Complaint simply does not allege trade dress infringement (See fn 2; see also Application, pp 19-20).

Pro-Seal also argues that packaging and labeling can be forms of trade dress, citing *Industrial Molding v Mfrs Mut Ins Co*, 17 F Supp 2d 633 (ND Tex, 1998), vacated at 22 F Supp 2d 569. (Resp, p 18). While that is undoubtedly true, it sheds no light on the inquiry whether the Flowserve Complaint asserts trade dress *infringement*. The notion that every complaint that alleges use of the plaintiff's packaging or label by the defendant asserts actionable trade dress infringement is directly contrary to the specific, well-established requirements for asserting a trade dress infringement claim. Indeed, Pro-Seal's description on page 18 of the conduct that it thinks triggered a defense obligation as alleged trade dress infringement is essentially identical to its description of conduct that it claims does not constitute trade dress infringement on page 5.

Pro-Seal also argues half-heartedly that allegations of trademark infringement necessarily encompass allegations of trade dress infringement, theorizing that the concept of trade dress is *broader* than the concept of trademark, that the concepts can sometimes be blurred, and that the Supreme Court has held that they are functional equivalents (Resp, pp 22-23). These arguments are soundly refuted in what appear to be the only cases that have addressed the issue, *StunFence*, *supra*, *NGK Metals*, *supra*, and *Albers Medical*, *supra*. Pro-Seal makes no attempt to address these cases or their unassailable reasoning, and cites no support from any jurisdiction in support of the Court of Appeals' finding that the Flowserve Complaint should be deemed to have alleged trade dress infringement.

⁵ Pro-Seal does not identify which of the Federal Rules of Civil Procedure would allow for the introduction of evidence of trade dress infringement and require "appropriate jury instructions," whatever that means. (Resp, pp 19-20). Nor does Pro-Seal explain the relevance of this test—much less cite any support for the proposition that courts should look to what evidence would be allowed, and what jury instructions would be required, to determine what claim is pled for purposes of an insurer's defense obligation.

Pro-Seal's argument that the supposed trade dress infringement allegations allege that the trade dress was in an advertisement is based on the unsupported contention that all trade dress infringement is advertisement by definition as "advertising" is commonly understood.⁶ (Resp, pp 18-19). Pro-Seal makes no attempt to address the actual language of the Citizens CGL Policy, including the definition of "advertisement," which is not surprising, since that language destroys its trade dress-involves-advertising-by-definition argument. Coverage exists only for "[i]nfringing upon another's . . . trade dress . . . in your 'advertisement.'" Obviously, if all trade dress were deemed advertisement by definition, this would read the "in your 'advertisement'" language out of the policy. (See additional argument at Application, pp 21-25).

Pro-Seal also argues that "the genesis of this case arose when an employee of Flowserve saw Flowserve's distinctive packaging at a third party vendor's place of business with the name Pro-Seal prominently displayed in red to anyone who would look at the item," and suggests based on this that Citizens' argument that there was no "advertisement" "loses touch with reality." (Resp, pp 18-19). Pro-Seal's "genesis of this case" statement, which is first made on page 4, is unsupported and should be disregarded. In any event, the notion that a mere label on a product or a distinctive package, even when combined with the placement of the product on a shelf, constitutes "a notice that is broadcast or published to the general public or specific market segment about your goods, products or services for the purpose of attracting customers or

⁶ The suggestion that all trademark/trade dress infringement inherently involves advertising generally, without reference to the definition of "advertisement" in the Citizens CGL Policy, is against the clear weight of authority. In addition to the cases that have discussed that point in the context of insurance coverage (see fn 8, *infra*), cases adjudicating Lanham Act claims have established that the Lanham Act "provides for two distinct causes of action: false designation of origin or source, known as 'product infringement,' and false description or representation, known as 'false advertising.'" *Resource Developers, Inc v Statue of Liberty-Ellis Island Found, Inc*, 926 F2d 134, 139 (CA 2, 1991). See also, *Cottrell, Ltd v Biotrol Intern, Inc*, 191 F3d 1248, 1252 (CA 10, 1999). The Flowserve Complaint alleges false designation of origin or source, i.e., product infringement, not false description or representation in advertising. (See Ct App Op, pp 4-5).

supporters” does not pass the straight-face test. That conduct does not even qualify as advertising under the ordinary meaning of that term, as cases have consistently held (See § C. below)—which is one reason why there is no coverage under the Citizens Excess Policy either.

The bottom line is that Pro-Seal simply has no response to Citizens’ argument that the Court of Appeals erred in applying the definition of “advertisement.” (Application, pp 21-26).⁷

C. There is no coverage under the Citizens Excess Policy

There are two reasons why there is no coverage under the Citizens Excess Policy. First, the allegations of trademark infringement in Flowserve’s Complaint are not allegations of “misappropriation of advertising ideas or style of doing business.” Although Pro-Seal disagrees with this proposition, and does cite decisions from other jurisdictions that agree with Pro-Seal on this point, there are only two cases that have applied Michigan law to such a question: *Advance Watch, Co v Kemper Nat’l Ins*, 99 F3d 795 (CA 6, 2002) and *Varilease Technology Group, Inc v Michigan Mut Ins Co*, 2004 WL 2913661 (Mich App). Both of those decisions support Citizens. Moreover, Pro-Seal incorrectly suggests that *Advance* stands alone against what should be considered the overwhelming authority on this point. At least two other federal courts have agreed with *Advance*: *Callas Enterprises, Inc v Travelers Indem Co of America*, 193 F3d 952 (CA 8, 1999), and *Nationwide Mut Ins Co v Mortenson*, 222 F Supp 2d 173 (D Conn, 2002).

Perhaps more importantly, Pro-Seal’s claim of coverage under the Citizens Excess Policy fails for the additional reason that the alleged trademark infringement was not causally connected

⁷ See also, *Transcontinental Ins Co v Jim Black & Assoc*, 888 So2d 671 (Fla App 2d Dist 2004) (although the insured allegedly engaged in demonstration of an infringing product, and claimant sought to prohibit "promotion" of product, there was no allegation of injury as a result of any notice that was broadcast or published); and *Scottsdale Ins Co v MV Transportation, Inc*, 2004 WL 726816, *4-5 (Cal App 2 Dist 2004), *rev’d only as to holding that insurer was not entitled to reimbursement of defense costs paid*, 36 Cal 4th 643 (**Exhibit B**) (rejecting insured’s argument that its focused and sequential approach to customers constituted "advertisement," defined as a notice that is broadcast or published to "general public" or "specific market segments").

to a “course of advertising.” The contention that it was, like the argument that the supposed trade dress infringement occurred in an “advertisement,” is premised on the thin reed that either (1) all trademark infringement necessarily involves advertising, or (2) the mere placement of a trademark-infringing label on a product, or a product in a trademark-infringing crate, constitutes advertising. For all its blustering about the “great body of law,” and the “overwhelming majority,” Pro-Seal’s response does not discuss one single case that supports the proposition that allegations of trademark infringement in the form of affixing a label or using a trademark-infringing container satisfies the “course of advertising” requirement.⁸

⁸ While the Court of Appeals cited *Poof Toy Products, Inc v United States Fidelity & Guaranty Co*, 891 F Supp 1228, 1235-1236 (ED Mich, 1995), as noted in Citizens’ Application the 6th Circuit in *Advance* rejected the *Poof Toy* reasoning. Indeed, the clear majority of cases to address the issue have held that the mere sale of a trademark-infringing product does not satisfy the requirement that there be a “course of advertising.” See, e.g., *Sport Supply Group, Inc v Columbia Casualty Co*, 355 F3d 453, 464-465 (5th Cir 2003) (holding, despite the fact that Texas has adopted broad definition of advertising, that merely affixing a label on a product to identify it is not “advertising”); *EKCO Group, Inc v The Travelers Indem Co of Ill*, 273 F3d 409, 414 (CA 1, 2001) (to define advertising to mean any form of calling public attention would be to “stretch the term ... in a way that has no natural stopping point short of absurd results”); *Farmington Cas Co v Cyberlogic Technologies, Inc*, 996 F Supp 695 (ED Mich 1998) (applying Michigan law to reject argument that product served to advertise itself, holding that such an approach would unreasonably expand scope of a CGL policy’s advertising injury coverage); *Century 21, Inc v Diamond State Ins Co*, 2004 WL 1117897, *4 (SDNY May 18, 2004) (**Exhibit C**) (merely selling an item does not constitute “advertising” as that term is used in an insurance policy and, thus, trademark infringement claim did not implicate advertising injury coverage); *Peerless Lighting Corp v American Motorists Ins Co*, 82 Cal App 4th 995, 98 Cal Rptr 2d 753, 764-66 (Cal App 1 Dist 2000) (rejecting argument that trademark and trade dress by their very nature constitute advertising for purposes of “course of advertising”); *Diversified Investments Corp v Regent Ins Co*, 596 NW2d 502 (Wis App 1999). Pro-Seal’s claim that there are “perhaps fifty reported cases” that support a finding of coverage in this case (Resp, p 14) is simply false. Pro-Seal is presumably referring to cases finding, contrary to *Advance, supra*, that trademark infringement can constitute “misappropriation of advertising idea,” of which there are quite a few (although probably not fifty). But that is unrelated to the separate “course of advertising” inquiry. Many of the cases identified in Pro-Seal’s “Appendixes” of cases do not support the propositions for which they are cited, and most if not all are distinguishable. For example, *Central Mut v Stunfence, supra*, is listed twice on Pro-Seal’s Appendix A. Not only did *Stunfence* not find advertising inherent in trademark/trade dress, the court specifically concluded that the mere attachment of trademark-infringing signs to products along with an attempt to pass them off as something else does not constitute advertisement. (See Application, p 26, fn 9.)

D. Coverage, if any, is precluded by the “with knowledge” exclusion

Even if there were coverage under either policy under the respective definitions of advertising injury, coverage is precluded by the “with knowledge” exclusion in the Citizens CGL Policy, which is made part of the Citizens excess policy through a follow-form provision (Application, Ex D, p 4). Pro-Seal’s argument regarding this exclusion is based primarily on an attempt to distinguish between “subjective knowledge” and an act committed intentionally. (See Resp., pp viii-ix, 29-35). Pro-Seal’s contention that this distinction “is elementary and beyond argument,” (Resp., p viii) is yet another criticism of the Court of Appeals opinion, which specifically notes that it was not addressing the distinction, “if such a distinction exists, between ‘knowledge’ and intent.” (Ct App Op, p 7, n 4). For present purposes, there is no meaningful distinction between knowledge and intent, as the Court of Appeals correctly found.

Pro-Seal’s argument, like so many of its arguments, makes no attempt to address the on-point cases cited in Citizens’ Application, all of which specifically hold that where the underlying complaint includes allegations of intentional wrongdoing, and does not include allegations of negligent or inadvertent wrongdoing, the “with knowledge” exclusion applies to preclude a defense obligation. See Application, pp 32-34 and cases discussed therein.

Assuming arguendo that the allegations in the Flowserve Complaint constitute allegations of personal and advertising injury, Pro-Seal cannot point to any allegation of conduct that was not undertaken with knowledge that the act would violate Flowserve’s rights and would cause that injury. Consequently, the Court of Appeals erred in finding that the “with knowledge” exclusion does not apply even if there was coverage in the first instance under either policy.

Respectfully submitted,

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